Conference of First Ministers on the Economy
Regina, Saskatchewan
February 14 - 15, 1985

CO-OPERATION FOR ECONOMIC EXPANSION

The Honourable Frank S. Miller
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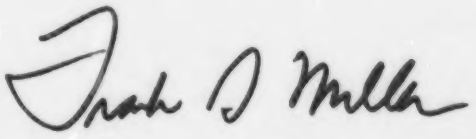
FOREWORD

I am confident that this Conference of First Ministers will begin a process in which governments and all sectors of Canadian society will work together to strengthen the national economy.

The federal and provincial governments have agreed on an agenda specifying major priorities for national attention. These are discussed in this paper. In each case, recommendations are put forward. I do not advance these recommendations as exhaustive answers to our problems; rather, they are suggested directions for change that, along with those of others, might guide our discussions so that we may better understand and agree upon common goals and actions for the future.



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I. Introduction

During the past two years, the Canadian economy has made significant progress. Almost 600,000 new jobs have been created. The inflation rate has been reduced by more than half; and real output has surpassed pre-recession peak levels. Indeed, the strength of Canada's recovery has been exceeded only in the United States and Japan.

A New Economic Environment

Economic recovery is continuing, but it is not business as usual. The economic environment has been fundamentally transformed. The most significant change is that inflation has been dramatically lowered. The rate of inflation has fallen from 12.5 per cent in 1981 to 4.4 per cent last year and likely will be below 4 per cent this year. In 1982, Canadian inflation was 4.7 points higher than the U.S. rate. This year, it is expected to be lower than in the United States.

There is every reason to believe that the victory over inflation can be a lasting one. Commodity prices are now steady or declining. The pattern of wage settlements over the last two years has been downward. Settlements averaged just over 3 per cent in the first three quarters of 1984 compared to 5.5 per cent in 1983. And productivity gains from improved technologies and better management techniques now offer scope for increased growth without rising prices.

Real interest rates, however, are currently higher than normal at this stage of recovery. Indeed, they have been persistently high for several years. This has contributed to the uneven growth of the economy.

CANADIAN REAL INTEREST RATES,* AFTER TWO YEARS OF RECOVERY
(Per cent)

Table 1

	Average of Recoveries Since 1950	Current Recovery 1984:4
Long-term bonds	3.3	8.2
Short-term paper	2.6	7.3
Prime	4.2	8.2

Source: Bank of Canada and Statistics Canada

* Real interest rates are calculated as the difference between the nominal rate and the year-over-year rate of change in the CPI for the quarter.

While export growth has been exceptionally robust, growth in consumer spending and business investment are below normal for this phase of recovery. A key assumption in the federal government's

projection for medium-term growth in Canada is that real interest rates will decline substantially and return to "more normal historical levels".

COMPARISON WITH PREVIOUS RECOVERIES
(Per cent change after 7 quarters of growth)

Table 2

	Average of Recoveries Since 1950	Current Recovery 1983:1 - 1984:3
Consumption	11.9	6.8
Business Investment in Plant & Equipment	9.7	-7.2
Exports	7.0	41.1
GNP	12.0	10.9

Source: Statistics Canada

The record on job creation has been good. In Ontario, the economy generated 156,000 new jobs over the past 12 months. Across the country, 264,000 new jobs were created. However, despite the strength of job creation, the nation's unemployment rate of 11.2 per cent remains unacceptably high. And several groups across the country face particular labour market problems; for example, young people, women, and older workers displaced by economic change.

Our priority for the future is clear. It is to create jobs by:

- encouraging investment;
- upgrading skills;
- building on regional strengths; and
- improving international competitiveness.

II. Encouraging New Investment to Create Jobs

The willingness to invest is the primary indication of the confidence of the business community. Moreover, investment improves efficiency and cost competitiveness while adding to productive capacity. It is essential to sustained job creation and a vigorous, expanding and internationally competitive private sector.

Recent Performance

Despite the relatively weak recovery of investment spending in Canada, the share of output devoted to private investment still compares favourably to that in other industrialized countries.

BUSINESS NON-RESIDENTIAL INVESTMENT IN MAJOR INDUSTRIAL COUNTRIES
(Per cent share of GDP)

Table 3

	Canada	United States	United Kingdom	West Germany	France	Japan
1970-73	13.2	12.0	12.8	13.0	14.0	18.4
1974-1981	15.0	12.8	12.9	11.5	13.3	16.4
1983[1]	13.0	12.0	9.3	11.9	11.1	17.1

Source: OECD and Statistics Canada
[1] Estimated

Investment spending has been improving in recent quarters; however, it remains inhibited by low capacity utilization rates. In addition, over-leveraged corporate balance sheet positions have constrained spending. Throughout the investment boom of the late seventies and early eighties, many firms financed their expansion with short-term, floating rate debt. To a large degree, they are now utilizing equity markets and retained earnings to pay down this debt rather than to add to plant capacity.

New Directions

Strong investment performance ultimately depends on continued growth in consumer demand and lower interest rates. Lower interest rates would also speed up the restructuring of corporate balance sheets by reducing the amount of cash that must be devoted to existing debt service charges.

Equally important is an improved climate of confidence for investors. In this regard, the federal government has made progress by proposing the establishment of Investment Canada to replace the Foreign Investment Review Agency.

Reducing the total burden of government deficits in Canada will also add to investor confidence and contribute to lower interest rates. Clearly this cannot involve merely shifting deficits from one level of government to another. Moreover, the deficit reduction process must be gradual in order to gain the maximum positive impact on sustaining the current economic expansion.

In the current environment, the overall performance of investment spending is unlikely to respond quickly to new general tax or grant incentives. Continued economic recovery along with the total financial support provided by existing policies and programs should provide sufficient incentive to invest. However, it is appropriate to review regulations and investment incentives to ensure that capital is being channelled into its most productive uses.

For example, the small business sector, the fastest growing sector of the economy, must have improved access to equity capital. This sector is being propelled by a large new generation of entrepreneurs, both men and women. With more efficiently designed incentives, it can continue to be the engine of growth and change.

There are successful programs currently in place, such as Ontario's Small Business Development Corporations Program. However, further progress can be made to rationalize incentives. In this respect, the federal government and the provinces are reviewing a number of changes in the personal income tax system that could improve the availability of equity capital to small firms.

Regulations governing financial institutions should also reflect the need to make debt and equity capital widely available at reasonable cost to Canadian businesses. These regulations are currently under review at both the federal and provincial levels. The federal government will shortly release its discussion paper, and the final report of the Ontario Task Force on Financial Institutions is due this fall. In addition to the priority of depositor and investor protection, these reviews should address the issue of increasing the availability of capital, in particular to small and medium-sized businesses. As well, pension fund criteria for eligible investments should be reviewed to determine if the access of small business to these very large pools of capital can be increased.

Technological innovation is a key element of the investment process. Adoption of new production processes and business techniques is particularly important to maintaining international cost competitiveness. Also, product innovations are critical to capturing new markets and maintaining traditional ones. A central element in meeting both of these objectives is to combine Canada's business and intellectual resources. Our colleges, universities and technology centres can become integrated into a continuum of scientific and business research, innovation, entrepreneurship, venture capital formation and job creation. In particular, the business community should be encouraged to become more

closely linked to our post-secondary educational institutions and to our technology centres for scientific and business research and training. The result can be a critical mass of growth and change for the whole economy.

Recommendations

- *As governments reduce their deficits, the federal government should pursue a monetary policy that encourages lower domestic interest rates, boosts household purchasing and stimulates investment.*
- *Government tax and expenditure policies should reinforce the trend to lower inflation expectations. However, reducing government deficits should not merely shift burdens from one level of government to another and should be gradual to reinforce the positive impacts on the current economic expansion.*
- *The current system of tax incentives should be examined to determine whether it encourages the most productive use of capital.*
- *Access by small business to equity capital should be improved.*
- *The review of regulations governing financial institutions should consider the cost and accessibility of capital to business, especially small and medium-sized business. Access to pension fund capital should be included in this review.*
- *Government policies should assist more rapid adoption of technology, particularly by small business.*
- *The business community should be encouraged to become more closely linked to post-secondary educational institutions for scientific and business research and training.*

III. Training Our Workforce

A skilled workforce helps reduce unemployment by making Canada a more attractive place in which to invest. At the same time, training enables Canadians to better adjust to the process of economic change.

A Shared Responsibility

Ensuring that all Canadians have access to training and educational opportunities is a shared responsibility. The provinces, with constitutional responsibility for education, have long had a central place in the delivery of training and retraining. The federal government, under the National Training Act, provides funding for both industrial and institutional training. Last year, 270,400 training places were provided under the NTA across Canada, of which 57,000 were on-the-job positions.

Co-operation between governments has always been necessary, both in delivering programs and in setting priorities. The federal government and the provinces must work together to ensure that regional and national goals are being achieved. Because resources have become more limited and economic change is more pervasive, it is now even more critical to avoid costly duplication and wasteful competition. In this regard, the large number of youth programs offered by both levels of government suggests that there is a real opportunity for governments to demonstrate a commitment to cost-effectiveness and program rationalization. It is also important to avoid gaps in the combined federal-provincial continuum of job creation and training programs.

Responsiveness and Flexibility

The federal allocation of training and job creation expenditures should be regionally balanced. Programs should be flexible enough to address the needs of the different regions and different stages of the business cycle. In some provinces, for example, shorter term job creation projects may be required. In Ontario, the current priority is for higher skills training, basic upgrading and a combination of training and job experience. Greater flexibility should also allow targetting on those groups whose needs for job experience, training or retraining are greatest.

A Focus on Youth

The youth unemployment rate has fallen from the recession high of 21.2 per cent. Yet at 17.6 per cent it remains totally unacceptable. The cost of youth unemployment is more than economic and more than temporary. It can be a lasting burden, both to the individual and to society.

A minority of unemployed young people experience repeated spells of unemployment of much longer duration than other workers. This group,

which accounts for a large proportion of the total time spent in unemployment, is characterized by low educational attainment and a lack of basic job skills. It is these young people who can especially benefit from skills development programs. Our aim must be to provide the combination of job experience, skills training, counselling and financial support that can enable them to earn a permanent place in the work force.

In recognition of changing priorities in the youth labour market, Ontario has undertaken a major restructuring of expenditures on youth programs. A new Minister responsible for Youth has just been appointed. He will co-ordinate and further develop youth programming. In addition, the Ontario government last year appointed a Youth Commissioner who is currently embarked on a mandate to strengthen training and practical experience in all youth programs and to put special emphasis on the needs of those young people whose employment problems are most severe.

Training for Older Workers

A second group that must be the focus of our training and retraining initiatives are older workers, particularly workers who have lost their jobs or whose jobs are threatened because of structural change and plant closure. Such workers frequently suffer prolonged periods of unemployment once they lose a job. As the baby boom ages, the number of youth in the labour force can be expected to decline, while the size of the older worker group will increase. At the same time, the demand for skills is changing as industry adapts in response to higher real capital costs, technological change, and foreign competition.

To help older unemployed workers acquire marketable skills, the Ontario Government now offers a special incentive to employers who hire and train laid-off workers over the age of 45. More can be done to address the unique problems of older workers under the National Training Act.

Women in the Economy

The increasing participation of women in the economy presents a unique set of issues which must be addressed by human resource policy. The labour force participation rate of women has grown from under 40 per cent in 1971 to about 53 per cent at present. In 1984, women made up 42.2 per cent of the Canadian labour force. Yet women remain predominantly in lower-paid occupations and industries. And unemployment rates for females, especially for older women, are higher than they are for males.

Governments must continue to encourage women to enter non-traditional occupations as well as new growth occupations. Special emphasis should also be placed on encouraging existing and potential women entrepreneurs. In addition, support for women re-entering the labour force could be enhanced as is currently provided under some parts of the National Training Act. Women can particularly benefit from bridging training that allows them to enter either employment or specific skills

Technical Upgrading Program. More can be done. Training opportunities could be further extended by offering more flexible scheduling and increased training allowances.

A Major Role for the Private Sector

While governments have an important role, labour and business must also take a major share of the responsibility for developing the skills of Canadian workers.

Firms can improve the productivity of the labour force not only by participating and cooperating with government programs, but also by developing and providing innovative training of their own. Indeed, recent studies have revealed that one characteristic of successful firms throughout the world is a strong and continuing commitment to improving the skills of their employees. Through training, individual firms can improve their own international competitiveness, as well as the skills of Canada's workforce.

Increasing the level of training also requires greater co-operation between business and labour. This is already occurring. Some unions, for example, have negotiated agreements which provide for the retraining of workers for new technologies. This should be encouraged.

Private sector training can help mitigate the effects of slowdowns in economic activity. If skills shortages are to be avoided during periods of strong economic growth, then advantage must be taken of private sector resources which may be idle during downturns.

Recommendations

- *Federal and provincial governments should cooperate to avoid duplication in the delivery and development of human resource programs. Towards this end, a list of possible candidates for program rationalization should be drawn up by each government.*
- *The labour market needs and priorities of the various regions must be recognized by the federal government in the development of new human resources initiatives and in the allocation of funds.*
- *Each of the provinces must receive a fair share of the allocation of federal training and job creation funding.*
- *The federal government should expand training opportunities provided under Section 39 of the Unemployment Insurance Act. (Section 39 provides for the payment of U.I. benefits to unemployed people in training programs).*
- *Employers and employees should be encouraged to co-operate to play a greater role in meeting their skill requirements.*

- *Governments should develop incentives for employers to hire and train workers with special needs such as the physically and mentally disabled.*
- *The recent Royal Commission on Equality in Employment should be an area of future consultations between the two levels of government.*
- *Government should assist displaced workers, especially older workers with dependents, by providing training allowances which take into account their income support needs.*
- *Part-time training programs should be expanded and training allowances provided.*
- *Technical upgrading programs under the National Training Act should be increased. Women can particularly benefit from bridging training that allows them to enter other employment or specific skills training programs.*
- *Through specific marketing strategies and counselling, public awareness of training programs for women should be increased.*
- *Emphasis should be placed on programs that support the entry of women into entrepreneurial activity.*
- *Federal and provincial governments should cooperate on a longer-term job-experience and training program for employment-disadvantaged young people.*

IV. Developing Canada's Regions

Furthering economic development in all parts of the nation has always been a first order priority of governments in Canada. It is an explicit commitment in the Constitution, and a cornerstone of Confederation.

Economic and Regional Development

Over the past decade, Ontario and other provinces have co-operated with the federal government in stimulating economic development through General Development Agreements. These Agreements have now been replaced with a new initiative. In recent months Ontario has signed an Economic and Regional Development Agreement (ERDA) with the federal government, as well as major sub-agreements covering forestry and tourism. The ERDA mechanism is an improvement on its predecessor in that it is more comprehensive and more flexible. Ontario will work jointly with the federal government on other ERDA initiatives.

Like other parts of the nation, Ontario has regions and communities that are largely dependent on a few primary resource industries, particularly in the northern and eastern parts of the province. Providing opportunities for diversification and strengthening of local economies in these areas is a high priority.

The ERDA program is not only a regional development initiative, but a process for co-operation on overall economic development throughout the nation. As such, it should have the flexibility to focus on any sector of the economy to raise productivity, foster growth, encourage rationalization and increase international competitiveness.

Effective regional development policies can only be achieved by close co-operation between Ottawa and the provinces. Accordingly, recent commitments by the federal government to assess its regional development policies and programs in consultation with provinces are welcome. Equally welcome are federal initiatives to avoid duplication and overlap in programs. However, a remaining obstacle to improved planning is that provinces do not know the funding levels that the federal government has available for economic and regional development within each province.

Reducing Disparity and Improving Competitiveness

The principles of regional economic development recently advanced by the federal government give due recognition to the importance of the nation's regional diversity and regional strengths. In this regard, the emphasis placed on sustainable economic activity based on realistic opportunities is essential. The viability of projects should be measured

against the need to remain competitive in the marketplace, both international and domestic.

Programs for regional economic development must strike an appropriate balance between the need to reduce disparities in economic opportunities and the need to ensure that the national economy improves its productivity and international competitiveness. The current federal initiative to re-assess economic development policies in this context is appropriate.

Community Initiative

New programs for regional development should also support the initiative of individual communities to foster new businesses. Programs should have maximum flexibility to build on local strengths. For example, in Ontario a new set of initiatives focussing on innovation centres, enterprise centres, new business spinoffs and community transformation agreements has been developed. These programs encourage entrepreneurship, taking into account local resources, needs and goals.

Recommendations

- *The ERDA should continue to be developed into a more general process of co-operative economic development, focussing on particular regions, industries and sectors.*
- *The federal government should establish and make public annually the funding available for new federal economic and regional development spending in each province.*
- *Policies to promote regional economic development should be based on regional strengths.*
- *Policies should be geared to supporting private sector efforts to improve productivity and strengthen domestic and international competitiveness.*
- *Program delivery mechanisms must be flexible and adaptable to a wide range of circumstances.*
- *Greater focus should be given to community sources of growth, especially through encouraging local entrepreneurship.*

V. Expanding International Trade

Challenges for Canada's Trade Policies

Canada is a trading nation. Exports account for about 30 per cent of GNP, a proportion similar to that of countries such as Germany, Italy, Britain and France.

Accordingly, Canada has played a leading role in negotiations to reduce international barriers to trade. For example, the average rate of duty on imports into Canada will have been reduced to about five per cent by 1987.

Today, Canada's trade policy challenges are:

- to secure the current degree of access to United States markets;
- to expand access to the United States on a mutually acceptable basis;
- to strengthen and extend the multilateral trading system; and
- to encourage Canadian businesses to take full advantage of opportunities for trade.

Securing Access to the United States Market

Canadian trade is overwhelmingly dependent on access to the United States market. In 1984, over 75 per cent of Canadian merchandise exports went to the United States. Over 90 per cent of these face very low tariffs, although there are significant non-tariff barriers. Canadian cost competitiveness has improved substantially over the past year and Canadian exports to the United States increased by 29 per cent in 1984. Accordingly, securing Canada's existing access should be the primary objective of our trade policy.

Therefore it is critical that Canada continue to strengthen efforts to fight new protectionist measures in the United States. Canada has been largely successful in recent months in presenting its case against such measures. However, the huge $123 billion United States trade deficit will continue to encourage protectionist sentiments.

In this regard, recent cases have demonstrated the importance of ensuring that the Canadian perspective, and those of allied United States interests, are persuasively and effectively made known to the United States Congress, the Administration and state governments. This requires co-operation and co-ordination between governments in Canada. But it cannot be done solely by governments; private enterprise must be actively involved as well. In addition to such actions, the possibility of a formal

bilateral trade agreement restricting the introduction of new tariff or non-tariff barriers should be explored.

Expanding Access

The issue of freer trade with the United States is again on the national agenda for discussion. The primary benefit of even greater access to the United States market is that increased economies of scale in production might help to increase Canadian productivity and lower costs. Over and above these gains, benefits could accrue from greater specialization. However, a major cost for Canada would be the disruption and reduction of economic activity during the process of restructuring. The magnitude and distribution of these costs would, of course, depend on the nature of the agreement.

Another major concern with entering into greater economic integration with the United States is the potential loss of political sovereignty. Greater access may require, for example, prohibition of policies to promote adjustment or economic development (including incentives related to R&D, marketing, exports, training, or investment), small business assistance and domestic procurement policies. Also, greater integration may reduce the ability of governments to manage the domestic economy. Clearly these are issues which require careful and complete study, including a full assessment of the associated costs and benefits.

A recent federal discussion paper outlines a number of possible approaches to achieving greater and more secure access to the United States market. Options include sectoral trade arrangements such as the Auto Pact, agreements covering only non-tariff barriers, a general framework agreement to address trade issues, or a comprehensive free trade agreement. Given the number, complexity and importance of the issues involved, the provinces should be extensively consulted on each of the options before any formal negotiations take place with the United States with the objective of achieving a bilateral agreement for free or freer trade.

Multilateral Trade Negotiations

The bilateral trade options with the United States should be weighed carefully against Canada's rights and obligations under the General Agreement on Tariffs and Trade (GATT). Moreover, efforts should continue to extend the GATT codes covering public sector purchasing policies, and support should be given to a new round of multinational trade negotiations. Combined efforts of several countries to seek modification or removal of protectionist policies should also be pursued. A recent example is the complaint to the GATT from Canada, the European Community and other countries against United States legislation to require country-of-origin markings on steel pipe.

Export Development

Canada's share of world exports declined to a low of 3.3 per cent in 1980. In 1983, it had recovered to 4.1 per cent. Canada must continue to build on this encouraging progress.

A national strategy for export development would help Canadian firms to take more effective advantage of the opportunities now available. Such a strategy should:

- maintain Canada's competitiveness with other industrial countries in the provision of export support;
- focus promotional efforts and set targets for high priority markets in the United States and the Pacific Rim;
- develop the export participation of small and medium-sized firms; and
- harmonize federal-provincial trade development programs and services.

Recommendations

- *Both the public and private sectors must work to ensure continued access to United States markets by strong representation of the Canadian viewpoint in the United States.*
- *The federal government should enter into extensive consultations with the provinces to give full and careful consideration to the implications of each of the options to increase access to the United States market.*
- *Canada should continue to support multilateral trade expansion through a new GATT round.*
- *A national trade strategy should be adopted which:*
  - *harmonizes federal-provincial trade development programs and services;*
  - *focusses promotional efforts and sets targets for high priority markets;*
  - *encourages the export participation of small and medium-sized firms;*
  - *maintains competitiveness with other industrial countries in the provision of export financing; and*
  - *encourages export consortia and strengthens market information systems.*

VI. Consulting on National Economic Priorities

At their annual conference in Charlottetown last August, the provincial Premiers signalled their desire for a renewed, co-operative approach to economic development in Canada. The new federal government has responded. Since last fall there has been an exceptionally active schedule of economic consultations between federal ministers and their provincial counterparts in the fields of finance, economic development, trade, training and technology.

Continuing Our Progress

The 1985 First Ministers' Conference on the Economy presents the opportunity to give further momentum to the continuing process of dialogue and cooperation among Canada's governments. First Ministers' Conferences can play a unique role in setting economic policy. They should be held annually to set directions, establish principles and review priorities.

Involving the Private Sector

At Premier Davis's initiative, Ontario hosted a major conference last September to strengthen partnership and increase dialogue among the leaders of industry, labour unions, municipalities, universities, and religious and community groups. It provided an opportunity for a free exchange of views on the province's economic future. The National Economic Conference in March will mark a similar approach. To be fully effective, these conferences should build on and be supported by regular tripartite consultations on key social and economic issues.

Intergovernmental consultation and private sector consultation should be seen as two concurrent and complementary processes. Partnership -- working together -- is not a new theme. But it is one that takes on new meaning and urgency in a world undergoing dramatic change. The active involvement of the private sector in the consultative process is essential.

Objectives

The objectives of the consultative process must be to build consensus, to increase public confidence and to expand the ability of governments, business and labour to secure stable and productive employment for Canadians. The test of the process will be its success in meeting these objectives.

Recommendations

- *A First Ministers' Conference should be held annually to review priorities, establish principles and set directions that will guide governments' decision-making.*
- *Intergovernmental consultations should be supplemented by private sector consultations that allow full participation by business, labour and governments. These consultations should give due regard to the regional nature of Canada's economy and to the respective powers of the federal and provincial governments.*